

Noncompete News: No Recovery of Compensation Tied to Unenforceable Noncompete

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In this edition of Noncompete News, we tackle two issues under Georgia law: (a) whether an employer can recover compensation paid to its employee in return for a restrictive covenant that is held to be unenforceable; and (2) whether an employer can recover salary it paid its employee if the employee violates its fiduciary duty or duty of loyalty owed to his employer during his employment. The Georgia Court of Appeals had an opportunity to address both of these issues recently in the insurance brokerage context.

A large insurance brokerage (the "Company") entered into an employment agreement with one of its vice presidents ("VP"). Pursuant to the agreement, the VP earned a salary and certain bonuses in exchange for selling professional liability insurance. The Company also paid the VP separate consideration in return for a nonsolicitation of customers provision.

After six years with the Company, the VP resigned and, the following day, began working for another insurance brokerage. The Company sued the VP for breach of contract, unjust enrichment, and breach of fiduciary duty/duty of loyalty.

The agreement sought to restrict the VP from "accept[ing] an entreaty from" any known or prospective customers. Following well-settled Georgia precedent, the Court determined the nonsolicit was unenforceable because, among other things, it prohibited the VP from accepting unsolicited business from a Company customer. The Company then sought to recover the money it paid the VP pursuant to the unenforceable nonsolicit. The Court rejected the Company's claim.

Quoting Georgia Supreme Court precedent, the Court held: "if an illegal contract be in part performed and money has been paid in pursuance of it, no action will lie to recover the money." The Court noted that the rule was "particularly appropriate where, as here, the party seeking equitable relief is the party who sought to benefit from the illegal contract, i.e., the illegal restraint of trade." Applying this rule, the Court concluded that the Company was precluded from pursuing the equitable remedy of unjust enrichment after entering into an illegal contract.

The Court elected, however, to uphold the jury's award in favor of the Company on the Company's breach of fiduciary duty claim. The evidence showed that, while still employed by the Company, the VP sought and obtained approval from an existing client to appoint him as the client's contact at the competitor's brokerage for whom he began working on the first business day after his resignation. The VP also established an e-mail account and telephone number at the competitor's brokerage and had printed invitations listing him as an employee of the competitor. Finally, the VP provided to the competitor price benchmarking information and information to reduce certain premiums to clients.

The Court held that, as both an officer of the Company as well as an employee, the VP

owed a fiduciary duty and a duty of loyalty to the Company. While this duty is not breached simply by making plans to enter a competing business while he was still employed, he was "not entitled to solicit customers for a rival business before the end of his employment nor could he properly do other similar acts in direct competition with the employer's business." The Court upheld the jury's award to the Company equal to two months of the VP's salary, in light of the VP's disloyalty to the Company during the last two months of his employment.

Bottom Line

The bottom line is this: Georgia Courts will not allow an employer to recover compensation paid to an employee in return for an otherwise unenforceable restrictive covenant, unless the agreement is controlled by another body of law (like ERISA). On the other hand, if the employee engages in unlawful competitive acts during his employment - - as opposed to competitive acts done after his employment ends - - the employer can recover compensation it paid to the employee during the time in which the employee breached his duties to the employer.